IN THE

United States Court of Appeals

FOR THE NINTH CIRCUIT

HOWFIELD, INC., formerly GALAXY, INC., *Appellant,*

vs.

UNITED STATES OF AMERICA, et al., *Appellees*

No. 22609

WILLIAM H. AHMANSON, as President of HOWFIELD, INC., etc., *Appellants*

vs.

UNITED STATES OF AMERICA, et al., *Appellees*

No. 22602

APPELLANTS' OPENING BRIEF

Consolidated Appeals from the United States District Court for the Central District of California

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STATUTES

SECTION 7602 OF THE INTERNAL REVENUE CODE OF 1954, AS AMENDED (26 U.S. CODE 7602)

Sec. 7602. Examination Of Books And Witnesses.

"For the purpose of ascertaining the correctness of any return, making a return where none has been made, determining the liability of any person for any internal revenue tax or the liability at law or in equity of any transferee or fiduciary of any person in respect of any internal revenue tax, or collecting any such liability, the Secretary or his delegate is authorized —

(1) To examine any books, papers, records, or other data which may be relevant or material to such inquiry;

(2) To summon the person liable for tax or required to perform the act, or any officer or employee of such person, or any person having possession, custody, or care of books of account containing entries relating to the business of the person liable for tax or required to perform the act, or any other person the Secretary or his delegate may deem proper, to appear before the Secretary or his delegate at a time and place named in the summons and to produce such books, papers, records, or other data, and to give such testimony, under oath, as may be relevant or material to such inquiry; and

(3) To take such testimony of the person concerned, under oath, as may be relevant or material to such inquiry."

SECTION 7604 OF THE INTERNAL REVENUE CODE OF 1954, AS AMENDED (26 U.S. CODE 7604)

Sec. 7604. Enforcement Of Summons.

"(a) Jurisdiction of District Court. — If any person is summoned under the internal revenue laws to appear,

to testify, or to produce books, papers, records, or other data, the United States district court for the district in which such person resides or is found shall have jurisdiction by appropriate process to compel such attendance, testimony, or production of books, papers, records, or other data.

(b) Enforcement. — Whenever any person summoned under section 6420 (e) (2), 6421 (f) (2), 6424 (d) (2), or 7602 neglects or refuses to obey such summons, or to produce books, papers, records, or other data, to give testimony, as required, the Secretary or his delegate may apply to the judge of the district court or to a United States commissioner for the district within which the person so summoned resides or is found for an attachment against him as for a contempt. It shall be the duty of the judge or commissioner to hear the application, and, if satisfactory proof is made, to issue an attachment, directed to some proper officer, for the arrest of such person, and upon his being brought before him to proceed to a hearing of the case; and upon such hearing the judge or the United States commissioner shall have power to make such order as he shall deem proper, not inconsistent with the law for the punishment of contempts, to enforce obedience to the requirements of the summons and to punish such person for his default or disobedience."

SECTION 7608 OF THE INTERNAL REVENUE CODE OF 1954, AS AMENDED (26 U.S. CODE 7608)

Sec. 7608. Authority Of Internal Revenue Enforcement Officers.

. . .

(b) Enforcement of Laws Relating to Internal Revenue Other Than Subtitle E. —

(1) Any criminal investigator of the Intelligence Division or of the Internal Security Division of the Internal

Revenue Service whom the Secretary or his delegate charges with the duty of enforcing any of the criminal provisions of the internal revenue laws or any other criminal provisions of law relating to internal revenue for the enforcement of which the Secretary or his delegate is responsible is, in the performance of his duties, authorized to perform the functions described in paragraph (2).

(2) The functions authorized under this subsection to be performed by an officer referred to in paragraph (1) are —

(A) to execute and serve search warrants and arrest warrants, and serve subpoenas and summons issued under authority of the United States;

(B) to make arrests without warrant for any offense against the United States relating to the internal revenue laws committed in his presence, or for any felony cognizable under such laws if he has reasonable grounds to believe that the person to be arrested has committed or is committing any such felony; and

(C) to make seizures of property subject to forfeiture under the internal revenue laws.

SECTION 2282 OF TITLE 28, UNITED STATES CODE.

Section 2282. Injunction against enforcement of Federal statute; three-judge court required

"An interlocutory or permanent injunction restraining the enforcement, operation or execution of any Act of Congress for repugnance to the Constitution of the United States shall not be granted by any district court or judge thereof unless the application therefor is heard and determined by a district court of three judges under section 2284 of this title."

SECTION 2284 OF TITLE 28, UNITED STATES CODE.

Section 2284. Three-judge district court; composition; procedure

"In any action or proceeding required by Act of Congress to be heard and determined by a district court of three judges the composition and procedure of the court, except as otherwise provided by law, shall be as follows:

(1) The district judge to whom the application for injunction or other relief is presented shall constitute one member of such court. On the filing of the application, he shall immediately notify the chief judge of the circuit, who shall designate two other judges, at least one of whom shall be a circuit judge. Such judges shall serve as members of the court to hear and determine the action or proceeding.

(2) If the action involves the enforcement, operation or execution of the State statutes or State administrative orders, at least five days notice of the hearing shall be given to the governor and attorney general of the State.

If the action involves the enforcement, operation or execution of an Act of Congress or an order of any department or agency of the United States, at least five days' notice of the hearing shall be given to the Attorney General of the United States, to the United States attorney for the district, and to such other persons as may be defendants.

Such notice shall be given by registered mail or by certified mail by the clerk and shall be complete on the mailing thereof.

(3) In any such case in which an application for an interlocutory injunction is made, the district judge to whom the application is made may, at any time, grant a temporary restraining order to prevent irreparable

damage. The order, unless previously revoked by the district judge, shall remain in force only until the hearing and determination by the full court. It shall contain a specific finding, based upon evidence submitted to such judge and identified by reference thereto, that specified irreparable damage will result if the order is not granted.

(4) If any such case the application shall be given precedence and assigned for a hearing at the earliest practicable day. Two judges must concur in granting the application.

(5) Any one of the three judges of the court may perform all functions, conduct all proceedings except the trial, and enter all orders required or permitted by the rules of civil procedure. A single judge shall not appoint a master or order a reference, or hear and determine application for an interlocutory injunction or motion to vacate the same, or dismiss the action, or enter a summary or final judgment. The action of a single judge shall be reviewable by the full court at any time before final hearing.

A district court of three judges shall, before final hearing, stay any action pending therein to enjoin, suspend or restrain the enforcement or execution of a State statute or order thereunder, whenever it appears that a State court of competent jurisdiction has stayed proceedings under such statute or order pending the determination in such State court of an action to enforce the same. If the action in the State court is not prosecuted diligently and in good faith, the district court of three judges may vacate its stay after hearing upon ten days notice served upon the attorney general of the State. As amended June 11, 1960, Pub.L. 86-507, Section 1(19), 74 Stat. 201."

REGULATIONS

Treasury Regulation 1118.6

"1118.6 *Intelligence Division.* The Intelligence Division enforces the criminal statutes applicable to income, estate, gift, employment and excise tax laws (except those relating to alcohol, tobacco, narcotics, and certain firearms), by developing information concerning alleged criminal violations thereof, evaluating allegations and indications of such violations to determine investigations to be undertaken, investigating suspected criminal violations of such laws, recommending prosecution when warranted, and measuring effectiveness of the investigation and prosecution process. The Division assists other Intelligence offices in special inquiries, drives and compliance programs and in the normal enforcement programs, including those combating organized wagering, racketeering and other illegal activity, by providing investigative resources upon regional or National Office request. It also assists U. S. Attorneys and Regional Counsel in the processing of Intelligence cases, including the preparation for and trial of cases."

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INTRODUCTION

FIRST ACTION — CASE NO. 22609

These cases involve essentially the same facts arising out of the same Internal Revenue Service investigation. Case No. 22609 (hereinafter referred to as first action), concerns a complaint (67-488-JWC, United States District Court for the Central District of California), filed by Howfield, Inc., formerly Galaxy, Inc., (hereinafter referred to as the taxpayer), which sought the return of seized property and the suppression of evidence under Rule 41(e) of the Federal Rules of Criminal Procedure. (22609 C.T. 2). (Hereinafter all references to the Clerk's

Transcript will be "C.T.", the Reporter's Transcript, "R.T." and each will be preceded by either 22609 or 22602). The basis for the relief sought by the taxpayer was the taxpayer's claim that its books and records were seized and copied by the government in violation of the taxpayer's constitutional rights. The government filed a motion to dismiss the taxpayer's complaint (22609 C.T. 29) which was initially denied but later was granted by the District Court on December 6, 1967. (22609 C.T. 226). The appeal in the first action is from that final judgment of dismissal. (22609 C.T. 232).

SECOND ACTION — CASE NO. 22602

Case No. 22602 (hereinafter referred to as the second action), involves an action commenced by the government, (67-489-JWC, United States District Court for the Central District of California), seeking enforcement of four Internal Revenue Service summons. (22602, C.T. 2). The taxpayer filed an answer thereto, a counterclaim seeking injunctive relief, and an application for the convening of a Three-Judge District Court. (22602 C.T. 57). The government filed an opposition to the application for a Three-Judge District Court. (22602 C.T. 60). The District Court dismissed the counter claim without leave to amend, and denied the application for a Three-Judge District Court on January 18, 1968. (22602 C.T. 83). The District Court determined that there was no just reason for delay in the entry of judgment and expressly directed that judgment be entered forthwith. (22602 R.T. 13, 311).

Thereafter, limited discovery was permitted (22602 R.T. 1-518), and a trial on the merits was held before a one judge District Court. The matter stands submitted pending the filing of post-trial briefs. The appeal

in the second case is from the judgment dismissing the counterclaim without leave to amend, and denying the application for a Three-Judge District Court. After Notice of Appeal was filed (22602 C.T. 85), the government moved to dismiss this appeal as frivolous and dilatory. This motion was denied by this court on April 2, 1968. Upon the joint motion of the parties, these cases were consolidated for purposes of briefing and argument.

STATEMENT OF ISSUES

1. In the first action, did the District Court err in determining that it had no jurisdiction to hear and determine the taxpayer's complaint under Rule 41(e) of the Federal Rules of Criminal Procedure seeking the return of property, and the suppression of evidence since there was no independent prosecution *in esse* at the time such complaint was filed?

2. In the first action, did the government's forcible return of the documents allegedly seized in violation of the taxpayer's constitutional rights after the taxpayer's complaint was filed, deprive the District Court of jurisdiction over taxpayer's complaint which sought both the return of illegally seized property as well as the suppression of illegally obtained evidence?

3. In the second action, did the District Court err in determining that it had no jurisdiction to hear the taxpayer's counterclaim for injunctive relief since there was an adequate remedy at law, and therefore that the taxpayer was not entitled to equitable relief?

4. In the second action, did the District Court err in failing to determine whether a substantial constitutional issue had been raised by the taxpayer's counterclaim for

injunctive relief and application for convening a Three-Judge District Court?

5. In the second action, did the District Court err in refusing to notify the Chief Judge of this Circuit, as required by Section 2284 of Title 28 of the United States Code, of the taxpayer's counterclaim and application for convening a Three-Judge District Court?

6. In the second action, had the taxpayer raised a substantial constitutional question in its answer and counterclaim so that the application for convening Three-Judge District Court should have been granted?

7. In the second action, did the District Court err in failing to make a determination whether the taxpayer's answer and counterclaim raised a substantial constitutional question?

STATEMENT OF THE CASE

These cases arise as a result of a nationwide criminal investigation conducted by the Intelligence Division of the Internal Revenue Service of the financing of political campaigns in the United States. This investigation which was officially known as "Operation Snowball", concerns the proper reporting of the receipt and disbursement of political contributions by public relations firms acting as campaign managers for political candidates and office holders, as well as whether non-deductible political contributions were illegally claimed as business expenses. (22602 R.T. 409, 411).

In the course of this investigation and in direct furtherance thereof, a series of Internal Revenue Service summons were issued to the taxpayer by a Special Agent of the Intelligence Division pursuant to Section 7602 of the Internal Revenue Code of 1954 (26, U.S.

Code). Initially, nine summons were served on the taxpayer as "a third party" in an alleged investigation of nine public relations firms named in said summons. After various portions of the taxpayer's records were produced in compliance with said summons, four new summons naming the taxpayer as the subject of an investigation were served upon the taxpayer. (22602 R.T. 372; C.T. 7-10). In the second action the government seeks judicial enforcement of these four summons. In both actions, the taxpayer alleged that it was actually the subject of a criminal investigation as much as four months prior to the service upon it of the nine summons directed to it as "a third party", and that as a consequence the government's access to its books and records was obtained through the exercise of fraud and deceit. In addition, the taxpayer further alleged that the primary function and purpose of the Special Agent of the Intelligence Division of the Internal Revenue Service who issued these summons was to investigate the taxpayer's suspected criminal violation of the Internal Revenue Code, and to obtain evidence of such suspected violation. Therefore, the four summons issued by the Special Agent were unenforceable since they were issued for the purpose of obtaining evidence for use in a criminal proceeding in direct conflict with the provisions of the Fourth Amendment to the Constitution.

After the taxpayer's complaint in the first action was filed, the government's petition in the second action was filed. Shortly thereafter, the documents supplied by the taxpayer to the government in response to the nine "third party" summons were forcibly returned by two Special Agents of the Intelligence Division to taxpayer's counsel. (22609 C.T. 96-100). Immediately thereafter, the government moved to dismiss the first action on the ground that since the taxpayer's documents had been

returned, this had the effect of changing the taxpayer's action to an action merely seeking the suppression of illegally obtained evidence. Accordingly, the government's argument concluded, since there was no prosecution *in esse,* the first action was not an independent proceeding over which the Court had jurisdiction. (22609 C.T. 29). This argument was rejected by the Court when initially presented. Later, however, apparently *sua sponte,* the Court granted the government's motion that no jurisdiction existed, and ordered that the second action, which had remained dormant during the pendency of the first action, should be reinstated. (22609 C.T. 226, 22602 C.T. 41).

Immediately thereafter, the taxpayer in the second action filed an answer, counterclaim seeking injunctive relief, and an application for a Three-Judge District Court. In both the answer and counterclaim, the taxpayer alleged that Section 7602 of the Internal Revenue Code, which authorizes warrantless searches and seizures in criminal tax cases, was violative of the Fourth Amendment and that Section 7602 was, therefore, unconstitutional. (22602 C.T. 48). The taxpayer sought to have the government permanently enjoined from utilizing such section as a basis for the issuance of summons directed to the taxpayer as well as to other third parties.

The District Court specifically refused to rule on whether a substantial constitutional question had been raised by the taxpayer. The Court made a determination that the taxpayer had not established that it was entitled to equitable relief since an adequate remedy at law existed. In this respect, the Court ruled that the adequate remedy at law consisted of the taxpayer's right to contest the action seeking the enforcement of the summons and if such resistance proved unsuccessful

at the trial, the right to pursue an appeal. (22602 R.T. 305-311). After the Court ruled that no just cause for delay existed for the entry of judgment, judgment dismissing the counterclaim was entered forthwith and this appeal was taken.

Trial in the second action was held before the District Court sitting without a jury in Los Angeles. The taxpayer's opening post-trial brief was filed on July 15, 1968. The government's answering brief is due on August 5, 1968, and the taxpayer's reply brief is due on August 19, 1968, at which time the matter in the District Court will stand submitted. If the taxpayer's contentions are correct that a Three-Judge District Court should have been convened, all of the District Court proceedings in the second action would appear to be nullity.

ARGUMENT

IN THE FIRST ACTION THE DISTRICT COURT HAD JURISDICTION TO HEAR AND DETERMINE THE TAXPAYER'S COMPLAINT THAT ITS RECORDS WERE SEIZED IN AN UNLAWFUL MANNER, AND THAT SAID RECORDS AS WELL AS ALL COPIES THEREOF SHOULD HAVE BEEN ORDERED RETURNED, AND ANY AND ALL EVIDENCE DIRECTLY OR INDIRECTLY OBTAINED THEREFROM SHOULD HAVE BEEN ORDERED SUPPRESSED AS EVIDENCE.

THE DISTRICT COURT HAD JURISDICTION

There is clear precedent in this circuit for the relief sought by the taxpayer in the first action. In *Goodman v. United States,* 369 F.2d 166 (9th Cir. 1966), this Court held that an action seeking the return of property and the suppression of evidence under Rule 41(e) of the Federal Rules of Criminal Procedure, was maintainable

even though the taxpayer had not been indicted at the time the action was brought. In its argument before the District Court, the government urged that since it returned the taxpayer's records after the taxpayer's complaint was filed, the taxpayer's action was thereby changed to one merely seeking the suppression of evidence which under *DiBella v. United States,* 369 U.S. 121, was a summary rather than an independent proceeding. Since there was no prosecution *in esse,* the government contended such an action was, therefore, not maintainable. The government distinguishes *Goodman* on the ground that in *Goodman,* the taxpayer's records had not been returned by the government.

The taxpayer contends that the government's construction of *DiBella* is incorrect since that case involved the question of an independent proceeding only INSOFAR AS APPEALABILITY was concerned. In *DiBella,* the Supreme Court merely held that an *appeal* from a judgment denying the return of property or suppression of evidence was maintainable, and would be considered an independent proceeding only if it was not tied to a prosecution *in esse.* The Court did not determine as the government incorrectly contends, that actions of the type brought by the taxpayer in the first action were not maintainable unless there was a prosecution *in esse.*

To the contrary, it is well established that an action seeking to enjoin the use of illegally obtained evidence may be brought prior to indictment, and that the District Court has jurisdiction to grant this relief. See *Burdeau v. McDowell,* 256 U.S. 465 (1921); *Perlman v. United States,* 247 U.S. 7 (1918); *Lapides v. United States,* 215 F.2nd 253 (2nd Cir. 1954); *Hoffritz v. United States,* 240 F.2nd 109 (9th Cir. 1956); *United States v. Rosenwasser,* 145 F.2nd 1015 (9th Cir. 1944).

THE FORCIBLE RETURN OF TAXPAYER'S RECORDS DID NOT DIVEST THE COURT OF JURISDICTION.

The government's further attempt to distinguish the instant proceedings from the above authorities on the basis of the self-help action of the two Special Agents, who in unbelievably clumsy fashion apparently attempted to cure any past wrongs by forcing taxpayer's counsel to accept certain documents and to sign a receipt therefor, is tenuous at best. (For a recitation of the action of the Special Agents in this respect see affidavit of Walter S. Weiss appearing at 22609 C.T. 96-100.)

In addition to the obvious observation that the heavy footed governmental investigator has no place in the American system of justice, and that the government should not be permitted through self-help to deprive the taxpayer of the right to contest the allegedly improper methods utilized in a criminal tax investigation, it is apparent that the return of the taxpayer's documents did not remove the information contained therein from the government's files. Certainly the government will not urge that the knowledge gained from the study of these documents was erased from the agents' minds. This philosophy was laid to rest many years ago in *Silverthorne Lumber Corp. v. United States,* 251 U.S. 385 (1920), where Justice Holmes stated:

> "The proposition could not be presented more nakedly. It is that although of course its seizure was an outrage which the government now regrets, it may study the papers before it returns them, copy them, and then may use the knowledge that it has gained to call upon the owners in a more regular form to produce them; that the protection of the Constitution covers the physical possession, but not any advantages that the government can gain over

the object of its pursuit by doing the forbidden act. *Weeks v. United States,* 232 U.S. 383, 58 L.ed. 652, L.R.A. 1915B, 834, 34 Sup. Ct. Rep. 341, Ann. Cas. 1915C, 1117, to be sure, had established that laying the papers directly before the grand jury was unwarranted, but it is taken to mean only that two steps are required instead of one. In our opinion such is not the law. It reduces the Fourth Amendment to a form of words. 232 U.S. 393. The essence of a provision forbidding the acquisition of evidence in a certain way is that not merely evidence so acquired shall not be used before the Court, but that it shall not be used at all."

In the first action the District Court should have permitted the taxpayer to establish not only the illegal methods employed by the government agents in the conduct of this investigation, but also that the information so obtained was being utilized in furtherance of a criminal investigation. The taxpayer was, and is, entitled to a return of its property in all respects which is illegally in the possession of the government. The District Court clearly had jurisdiction, and it erred in dismissing the taxpayer's complaint in the first action.

IN THE SECOND ACTION THE TAXPAYER'S COUNTERCLAIM FOR INJUNCTIVE RELIEF RAISED A SUBSTANTIAL CONSTITUTIONAL QUESTION WHICH REQUIRED THE DISTRICT COURT TO NOTIFY THE CHIEF JUDGE OF THIS CIRCUIT SO THAT A THREE-JUDGE DISTRICT COURT COULD HAVE BEEN CONVENED.

THE DISTRICT COURT HAD ONLY LIMITED AUTHORITY

Section 2284 of Title 28 of the U.S. Code provides that when an appropriate attack is made upon a statute of

the United States on the grounds of unconstitutionality, the District Court must immediately notify the Chief Judge of the Circuit who is then required to convene a Three-Judge District Court. The Three-Judge District Court determines all of the issues raised by the pleadings, both constitutional and otherwise. *Zemel v. Rusk,* 381 U.S. 1, 6 (1965).

The Supreme Court has repeatedly held that the only determination which the one judge District Court may make is whether the constitutional issue raised was patently insubstantial. *Zemel v. Rusk, supra; Idlewild Bon Voyage Liquor Corp. v. Epstein,* 370 U.S. 713 (1962); *Schneider v. Rusk,* 372 U.S. 224 (1963).

If the District Court makes the determination that the constitutional attack is not patently insubstantial, the District Court has no authority other than to notify the Chief Judge of the Circuit and the complainant, as a matter of right, is entitled to have the matter heard by a Three-Judge District Court. The District Court must act in this fashion notwithstanding the fact that the District Court believes the statute being attacked is constitutional. *Zemel v. Rusk; Idlewild Bon Voyage Liquor v. Epstein; Schneider v. Rusk.*

In *Schneider v. Rusk,* the Supreme Court stated:

> "Trial of this case should have been before a Three-Judge District Court convened pursuant to 28 U.S.C. Sections 2282, 2284, as petitioner requested. Her complaint explicitly sought an 'injunction restraining the enforcement, operation or execution of . . . [an] Act of Congress' — Section 352(a)(1) of the Immigration and Nationality Act of 1952, 8 U.S.C. Par. 1484(a)(1), which provides that a naturalized American citizen shall lose his

nationality by 'having a continuous residence for three years in the territory of a foreign state from which he was formally a national or in which the place of his birth is situated . . .'"

. . .

"Although no view is here intimated as to the merits of the constitutional question in the present case, we disagree with the conclusion of the courts below as to the substantiality of that issue".

. . .

"The single judge District Court was therefore powerless to dismiss the action on the merits, and should have convened a Three-Judge Court." (Emphasis added.)

In *Idlewild Bon Voyage Liquor Corp. v. Epstein,* at p. 715, the Supreme Court said:

"When an application for a statutory Three-Judge Court is addressed to a District Court, the court's inquiry is appropriately limited to determining whether the constitutional question raised is substantial, whether the complaint at least formally alleges a basis for equitable relief, and whether the case presented otherwise comes within the requirements of the Three-Judge statute. Those criteria were assuredly met here, and the applicable jurisdictional statute therefore made is impermissible for a single judge to decide the merits of the case, either by granting or by withholding relief."

SECTION 7602 IS PATENTLY UNCONSTITUTIONAL

In support of the contention that Section 7602 is an impermissible attempt to circumvent the Fourth Amend-

ment, the taxpayer relies upon the Internal Revenue Code (Section 7608), the Treasury Department's own regulations (Treas. Reg. 1118.6), the decided cases (*Mathis v. United States,* ..... U.S. ....., 20 L.Ed.2d 381; *United States v. Gower,* 271 F. Sup. 655 (N.D. Pa. 1967); *United States v. Caplan,* 255 F. Sup. 805 (E.D. Mich. 1966); *United States v. Kleckner,* 273 F. Sup. 251 (S.D. Ohio 1967); *United States v. Wainwright,* ..... F. Sup. ....., 21 AFTR 2d 1039 (D.C. Colo. 1968)), and the testimony of both present and former Internal Revenue Service personnel (22609 R.T. 35, Appendix, *infra*). All of these authorities make it abundantly clear that the *primary* function of a Special Agent of the Intelligence Division is to investigate possible criminal violations of the Internal Revenue Code, and to obtain evidence thereof for use in subsequent criminal proceedings.

It is equally abundantly clear that the summons issued by the Special Agent in this investigation was an attempt to carry out this primary function to obtain evidence for use in the prosecution of the taxpayer. The taxpayer submits that if it can be established that, (1), this statute may be construed to authorize the conduct of criminal tax investigations by the use of summons designed to avoid the requirements of obtaining the approval of a neutral and detached judicial officer prior to the compulsory production of a taxpayer's books and records, or (2), the statute has been utilized in such a widespread fashion by an investigative instrumentality of the United States, it is in patent conflict with the Fourth Amendment.*

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* (Although it is recognized that evidence produced at the hearing before the District Court commencing on May 7, 1968 is not a part of the official record in these proceedings, in light

THE CRIMINAL INVESTIGATORS OF THE INTERNAL REVENUE SERVICE ARE SUBJECT TO THE SAME RESTRICTIONS AS ALL OTHER FEDERAL CRIMINAL INVESTIGATORS.

In light of the foregoing and the material set forth in the Appendix, it is submitted that the government, occupying the position of being more than merely a litigant before this Court, must now concede that the summons which it is seeking to have ordered enforced were issued for the principal purpose of obtaining evidence of a suspected criminal violation of the Internal Revenue laws by the taxpayer.

In the past it has been the government's consistent position that only if the taxpayer could establish that the *sole* purpose of a Special Agent conducting a tax investigation was the obtaining of evidence for use in a criminal proceeding would it be improper for a summons

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of the clear insight revealed into the true nature of this investigation by such proceedings, various portions of the reporter's transcript in those proceedings are set forth in the attached appendix to this brief. These attachments consist of a portion of the testimony of Mr. Thomas Sullivan, a senior trial attorney with the Internal Revenue Service who was formerly Assistant Regional Counsel-Enforcement, and who was the Internal Revenue Service attorney who advised and assisted in the preparation of the four summons which the government seeks to have enforced in the second action; a memorandum dated October 25, 1966 prepared by Special Agent Gabriel Dennis which was addressed to All Audit and Intelligence Personnel Concerned in the Southern California Area; and a portion of a memorandum dated February 13, 1967 prepared by Intelligence Division Group Supervisor Vernon Hansen which was addressed to The District Director of Internal Revenue, Los Angeles, California and which was entitled "Investigation of Political Contributions Deducted as Business Expenses.")

under Section 7602 to be issued. The government's logic then concluded that since the Special Agent is never certain that his investigation will result in a criminal prosecution, and further, since the civil aspects of the case are always pursued at the conclusion of the criminal aspects of the case, these factors demonstrate that the Special Agent's investigation is not conducted *solely* for the purpose of obtaining evidence for use in a criminal proceeding. The taxpayer submits that both the premise and conclusion are erroneous, and the authorities relied upon by the government are no longer valid.

The taxpayer submits that the only appropriate test to be applied is not whether the *sole* purpose for the issuance of the summons was the obtaining of evidence for use in a criminal proceeding, but rather whether this was the *principal* or *primary* purpose. The reason for this is obvious since if the sole purpose test is utilized it could be avoided simply by adding a corollary purpose of relative insignificance. Since the presence of such an insignificant secondary purpose could be completely within the government's control, it is obvious that any test other than the principal purpose test would be meaningless and easily circumvented.

The government's contention that when a summons was issued, the Special Agent was not yet convinced that a crime had been committed and that therefore the issuance of the summons was not for the purpose of obtaining evidence for use in a prosecution *in esse,* is similar to that raised in *Camara v. Municipal Court,* 387 U.S. 523 (1967) and *See v. Seattle,* 387 U.S. 541 (1967). In rejecting these arguments the Supreme Court stated in *Camara,* at p. 530-531:

> "It is surely anomalous to say that the individual and his private property are fully protected by the

> Fourth Amendment only when the individual is suspected of criminal behaviour. For instance, even the most law-abiding citizen has a very tangible interest in limiting the circumstances under which the sanctity of his home may be broken by official authority, for the possibility of criminal entry under the guise of official sanction is a serious threat to personal and family security."

In *See,* the rule in *Camara* was extended to include commercial premises. There the Court stated at p. 543:

> "Likewise, we see no justification for so relaxing Fourth Amendment safeguards where the official inspection is intended to aid enforcement of laws prescribing minimum physical standards for commercial premises. As we explained in *Camara,* a search of private houses is presumptively unreasonable if conducted without a warrant. The businessman, like the occupant of a residence, has a constitutional right to go about his business free from unreasonable official entries upon his private commercial property. *The businessman, too, has that right placed in jeopardy if the decision to enter and inspect for violation of regulatory laws can be made and enforced by the inspector in the field without official authority evidenced by a warrant".* (Emphasis supplied).

It should further be noted that there is a clear tendency by the Supreme Court to construe the Fourth Amendment expansively, and in reaching its decisions in both *Camara* and *See,* the Court expressly overruled its prior decision in *Frank v. Maryland,* 359 U.S. 360. Furthermore, the government cannot seriously urge that the Court was required to determine whether the housing inspector in *Camara,* and the fire inspector in *See,* were

solely seeking evidence for use in a criminal proceedings. This is simply not determative of when or whether a search warrant is required prior to an involuntary search. The Court stated in *Camara* at p. 531: "Like most regulatory laws, fire, health, and housing codes are enforced by criminal processes." This fact, the Court reasoned required that the safeguards of the warrant procedures must be followed. This reasoning is fully applicable in the instant proceedings.

The taxpayer submits that the archaic and deceptive "sole purpose test" so heavily relied upon by the government in the past, has now been thoroughly discredited and is no longer persuasive.

Although the investigating agents in this case have been candid enough to admit that their investigation known as "Operation Snowball" was not a "routine tax investigation", but rather was designed to determine whether criminal violations of the tax laws had occurred (22602 R.T. 313-317, 394-398), in *Mathis v. U.S.,* the Supreme Court placed even "routine tax investigations" within the *Miranda* rule. There the Court stated:

> "It is true that a 'routine tax investigation' may be initiated for the purpose of a civil action rather than criminal prosecution. To this extent tax investigations differ from investigations of murder, robbery, and other crimes. But tax investigations frequently lead to criminal prosecutions, just as the one here did. In fact, the last visit of the revenue agent to the jail to question petitioner took place only eight days before the full-fledged criminal investigation concededly began. And as the investigating revenue agent was compelled to admit, there was always the possibility during his investigation that his work would end up in a criminal prosecu-

tion. We reject the contention that tax investigations are immune from the *Miranda* requirements for warnings to be given to a person in custody."

The taxpayer submits that in the instant case, where the facts are far stronger insofar as the primary criminal nature of the investigation is concerned, the demand for access to respondents' books and records without a warrant flies clearly in the face of these pronouncements by the Supreme Court, and the statute which purportedly authorizes such action is patently unconstitutional. Furthermore, the taxpayer is without an adequate remedy at law and is therefore, entitled to the equitable relief prayed for in its counterclaim.

Notwithstanding the cogency of the foregoing material which demonstrates otherwise, the government with questionable candor has consistently urged that Special Agents of the Intelligence Division are something other than criminal investigators.

In *United States v. Gower,* the Court, after first referring to Treasury Reg. 1118.6, characterized the Special Agent of the Intelligence Division as the "Police arm of the Internal Revenue Service" who conducts "inquiries for possible criminal violation". The Court in *Gower* also pointed out that Sections 7601 through Section 7606 of the Internal Revenue Code conferred *civil audit* power on Internal Revenue Agents. This distinction between the civil audit powers and functions of Internal Revenue Agents of the Audit Division, and the criminal investigative power and functions of Special Agents of the Intelligence Division, has been consistently denied by the government. In this case, the summons were not issued by an Internal Revenue Agent of the Audit Division for the purpose of performing a civil audit. They were not issued by a Special Agent of the Intelligence Division for

the purpose of conducting a civil audit. They were issued by a Special Agent for the primary purpose of obtaining evidence for use in a criminal proceeding against the taxpayer.

As indicated above, the recent Supreme Court decision in *Mathis v. United States,* considered the argument advanced by the government that a routine tax investigation *conducted by a Revenue Agent was* outside the scope of *Miranda,* since *"no criminal proceedings might ever be brought"*. This substantially identical argument is asserted by the government in these proceedings. (The government also urged in *Mathis* that *Miranda* should not apply since the taxpayer being questioned had not been put in jail by the officers questioning him). In brushing aside these arguments, Justice Black stated that these differences were "too minor and shadowy to justify a departure from . . . " *Miranda.* Respondents submit that the government's contentions in this case are likewise "too minor and shadowy to justify a departure from" the fundamental Fourth Amendment requirements that investigating police officials may not have the unrestricted right to demand access to, or the production of, books and records without the prior specific approval of an independent judicial officer. The government's stubborn refusal to admit that the Special Agent was seeking evidence for use in a criminal proceeding based on its minor and shadowy contentions should now be laid to rest once and for all.

The clearly recognized distinction between the civil functions of an Internal Revenue Agent and the criminal functions of a Special Agent are set forth in footnote 2 of the dissent in *Mathis* where it is stated:

> "A civil investigator is required, whenever and as soon as he finds 'definite indications of fraud or

> criminal potential,' to refer a case to the *Intelligence Division for investigation by a different agent who works regularly on criminal matters.* In the case before us, such a reference was made 8 days after the second visit to petitioner by (Internal Revenue) Agent Lawless. The *criminal agent* visited petitioner, gave him the full set of 'Miranda warnings,' and was told petitioner did not wish to discuss the case with him. No further questions were asked." (Emphasis supplied.)

IN THIS APPEAL ALL THE ALLEGATIONS OF THE COUNTERCLAIM MUST BE ACCEPTED AS TRUE.

Irrespective of whether the "sole purpose" or "principal purpose" test is utilized, on this appeal this Court is bound to accept all of the allegations of the counterclaim as true. All of the material allegations of a pleading, dismissed without leave to amend, and all reasonable inferences that may be drawn from the pleading must be taken as true. *Clark v. Uebersee Finanz-Korporation A.G.,* 332 U.S. 480, 482 (1947). Such a pleading must be liberally construed and must be sustained except where it is certain that the pleader would not be entitled to relief under any state of facts which could be proved in its support. *Leimer v. State Mutual Life Assur. Co.,* 108 F. 2d 302, 306 (9th Cir. 1940). Justice Frankfurter's warning in *Eccles v. People's Bank of Lakewood Village,* 333 U.S. 426, 432 (1948) is pertinent here:

> ". . . Caution is appropriate against the subtle tendency to decide public issues free from the safeguards of critical scrutiny of the facts . . ."

Accordingly, for the purposes of this appeal this Court must take as facts the following (1) so far as this taxpayer is concerned, "Operation Snowball" constituted a

criminal investigation of this taxpayer and only a criminal investigation of this taxpayer, (2) that those summons that were issued were issued in furtherance of the criminal tax investigation of the taxpayer, and (3) that such further summons as might be issued, the issuance of which the counterclaim sought to enjoin, would be issued in furtherance of the criminal tax investigation of the taxpayer.

A SECTION 7602 SUMMONS IS NOT A VALID SUBSTITUTE FOR A SEARCH WARRANT.

The summons involved in these proceedings are similar not only to the subpoena condemned in *Pollard v. Roberts,* 283 F. Sup. 248 (E.D. Ark. 1968), but also to the subpoena involved in *Mancusi v. De Forte,* ..... U.S. ....., 36 Law Week 4682 (June 18, 1968). In *Mancusi,* a district attorney's subpoena was issued which required the production of certain books and records of a labor union. In holding that the subpoena was not equivalent to a validly issued search warrant, the Court stated at p. 4684:

> "Moreover, the subpoena involved here could not in any event qualify as a valid search warrant under the Fourth Amendment, for it was issued by the District Attorney himself, and thus omitted the indispensable condition that 'the inferences from the facts which lead to the complaint' . . . be drawn by a neutral and detached magistrate instead of being judged by the officer engaged in the often competitive enterprise of ferreting out crime.' Johnson v. United States, 333 U.S. 10, 14. Giordenello v. United States, 357 U.S. 480, 486."

In light of the foregoing pronouncements, it is submitted that if it is determined that Congress intended by Section 7602 to confer the unrestricted inquisitorial power which the government seeks to have enforced, said section is patently unconstitutional, since it is in direct contravention of the Fourth Amendment. On the other hand, if the section is being relied upon by the government to permit its criminal investigators to obtain evidence in furtherance of criminal investigations, then the widespread use of this section by the government in this fashion is likewise constitutionally impermissible. In either event, however, since this constitutional issue was properly raised by the taxpayer, a Three-Judge District Court should have been convened to determine the constitutionality of the challenged statute. In addition, the taxpayer should have been granted the equitable relief which it sought.

Respondents further submit that the power which the government contends resides in the Commissioner of Internal Revenue by virtue of Section 7602, is further constitutionally impermissible. By claiming the authority to issue Section 7602 summons to obtain evidence of possible criminal violations of the Internal Revenue Code, the decision of whom to investigate and possibly whom to prosecute has been attempted to be moved to a branch of the executive department, in Washington, D. C., free from the supervision and control of local Courts and local grand juries. When the particularly sensitive nature of this investigation is considered, the reason for the well recognized prohibition against such central authority becomes obvious. Although in the instant proceedings, the taxpayer does not necessarily suggest that the present Commissioner of Internal Revenue is acting in a discriminatory or unfair fashion, the test of impermissible power is not measured by whether

it is being fairly exercised, but rather whether in the absence of adequate safeguards, it may be unfairly applied. The element of fairness is insured by the presence of the supervision by either the Court or the grand jury, historically the only legitimate instrumentalities with processes to compel the production of evidence for use in criminal proceedings.

For the latest reported decision concerning the special significance of investigations of the financing of political campaigns, the Court's attention is respectfully invited to *Pollard v. Roberts,* 283 F. Supp. 248 (E.D. Ark. 1968). Although that case turned on the application of the First Amendment to the Constitution, the case nevertheless points out the dangers resulting from a public agency or officer being permitted to inhibit or discourage unreasonably the meaningful participation of citizens in American political life. As pointed out in *Pollard,* since such an incredible area of abuse is possible, all criminal investigations of political finance must be particularly scrutinized and supervised by the independent judiciary.

A SECTION 7602 SUMMONS ISSUED BY A SPECIAL AGENT IS UNENFORCEABLE.

An area of confusion with respect to the taxpayer's position has perhaps been caused by the peripheral application of *Miranda* and *Escobedo.* In those cases, it has been held that before a suspect is required to be advised of his right to counsel, the accusatory, as distinguished from the investigative stage of an investigation, must have been reached. In *Miranda* this was explained to have occurred when the person had been taken into custody or otherwise deprived of his freedom of action in any significant way. It is the consistent

position of the government that a tax investigation being conducted by a Special Agent of the Intelligence Division does not become a criminal investigation until some restraint upon the taxpayer has been imposed. Thus in the *Kohatsu* situation, for example, *Kohatsu v. United States,* 351 F.2d 898 (9th Cir. 1965), the government successfully urged that the taxpayer there was not entitled to a warning of his constitutional right to counsel since he had been neither arrested nor indicted.

It is not the principal thrust of the taxpayer's argument in this case that the summons here involved are not enforceable because of a failure on the part of the government to comply with the requirements of *Miranda.* Rather, the taxpayer contends that if summons are issued by a Special Agent in the course of his official duties, they are issued for the primary purpose of obtaining evidence for use in a criminal proceeding and are, therefore, unenforceable since the statutory authority for their issuance is unconstitutional. It is completely irrelevant whether or not the taxpayer is in custody, or deprived of his freedom of action in some significant way, when the summons are issued. As indicated in *Camara,* neither custody nor suspicion are required prior to the applicability of the Fourth Amendment.

The taxpayer submits that in the second action it has raised in the pleadings a substantial constitutional question which could only be considered by a Three-Judge District Court. The District Court patently erred in dismissing the taxpayer's counterclaim, denying the taxpayer's application for Three-Judge District Court, and conducting a one judge trial on the merits.

CONCLUSION

In the first action the taxpayer submits that the District Court erred in dismissing taxpayer's complaint seeking the return of illegally seized property and the suppression of illegally obtained evidence.

In the second action the taxpayer submits that it properly raised a substantial constitutional issue and that the District Court erred in dismissing the taxpayer's counterclaim for injunctive relief, in denying the taxpayer's application for a Three-Judge District Court, and in denying the equitable relief sought.

Respectfully submitted,

GOODSON AND HANNAM
and
WALTER S. WEISS

Walter S. Weiss
Wm. E. Hannam
Counsel for Appellants

APPENDIX

Portion of testimony of Thomas J. Sullivan given on May 9, 1968 in U.S. et al v. Ahmanson, No. 67-489-JWC, U.S. District Court, Central District of California, which appears at Reporter's Transcript of the Proceedings, pages 278-279:

"BY MR. WEISS:

Q Do you know whether Mr. Dennis was conducting a civil or a criminal investigation of Galaxy on January 30th when he had this visit with you and showed you the summons?

A He was conducting an examination that could go either way.

Q That I would like you to explain. You mean it could ultimately wind up in a prosecution?

A Right.

Q Or it could wind up in merely civil tax or it might wind up with two taxes?

A That's right, Mr. Weiss.

Q Is that correct?

A That's correct.

Q What was his primary function.

MR. UGAST. If he knows, Your Honor.

MR. WEISS: If he knows.

THE WITNESS: The primary function of a special agent is to investigate possible criminal violations of the Internal Revenue laws."

October 25, 1966

"All Audit and Intelligence Division Personnel Concerned:

October 25, 1966
Acting Chief, Audit Division
Chief, Intelligence Division:
Political Contributions — Operation Snowball.

"An investigation currently being conducted by the Intelligence Division for the years 1962 through 1965 has uncovered evidence that individuals and corporations are taking non-deductible political contributions as business expenses.

"The evidence shows that public relations firms represent various political candidates in obtaining contributions for political campaigns. A scheme has been devised whereby corporations and individuals who wish to make substantial contributions to a political candidate are told that they will be furnished an invoice billing them for 'Advertising Expense,' 'Consultation,' 'Public Relations Services,' et cetera, in the amount of their contribution. They are told that the invoices can then be used as business deductions for income tax purposes.

"The public relations firms then make arrangements with advertising and printing companies whereby these companies submit what appear to be regular invoices for advertising and/or printing to the corporations or individuals making the political contributions.

"The evidence also shows that various political contributors have been receiving billings from various firms of attorneys to cover their political contributions. The contributor receives a billing from an attorney which is indicated as being for 'Advanced Costs' and/or 'Re-

tainer,' The contributor then issues his check in the name of the attorney who deposits these checks to his 'Trust Account.' The attorney then issues a check from the trust account to the designated political campaign. By this method the contributor makes a political contribution and takes a deduction on his books for legal fees.

"It is requested that all Internal Revenue Agents in the Los Angeles District be alerted that in the course of their examinations if they discover payments being made to the following companies and/or attorneys (Payments to attorneys usually are in even amounts of $500 and/or $1,000), they immediately notify Special Agent Gabriel Dennis, Ext. 4247, or Vern F. Hansen, Supervisor, Ext. 4256."

Public Relations Firms:

(9 names omitted by direction of Court)

Advertising Firms:

GALAXY ADVERTISING, INC.

(10 names omitted by direction of Court)

Printing Firms:

(7 names omitted by direction of Court)

Attorneys:

(13 names omitted by direction of Court).

(Signed)
Chester B. Parnell,
Acting Chief,
Audit Division
Robert K. Lund,
Chief,
Intelligence Division

(22602 R.T. 340-342) (Reporter's Transcript of Proceedings of May 8, 1968, p. 176-178, U.S. v. Ahmanson, 67-489-JWC, U.S. District Court, Central District of California).

PORTION OF MEMORANDUM DATED FEBRUARY 13, 1967 TO THE DISTRICT DIRECTOR OF INTERNAL REVENUE ATTENTION CHIEF INTELLIGENCE DIVISION LOS ANGELES, CALIFORNIA FROM V. F. HANSEN, GROUP SUPERVISOR, LOS ANGELES, CALIFORNIA WHICH APPEARS AT PAGES 14-15 OF REPORTER'S TRANSCRIPT OF PROCEEDINGS OF MAY 7, 1968 IN U.S. ET. AL. v. AHMANSON, NO. 67-489-JWC, U.S. DISTRICT COURT CENTRAL DISTRICT OF CALIFORNIA.

"At our request, a meeting was held with representatives of the Office of Regional Counsel. The facts were explained to the representatives of Regional Counsel and they were told that although the original summonses which had been issued in this case had not been honored, we were now in the position that GALAXY, INC. should be investigated for possible criminal violations of the Internal Revenue Code. As a result of that meeting, on January 26, 1967, I made an assignment to Special Agent GABRIEL DENNIS for an unnumbered investigation of GALAXY, INC. and new summonses were drawn up with the approval of Regional Counsel and were served on representatives of GALAXY, INC. on January 31, 1967. The new summonses clearly state that they are being issued in connection with an investigation of GALAXY, INC. (separate summonses were issued for the open and closed years)."